CHANDLER ASSET MANAGEMENT

Economic highlights from the week ending on August 20, 2021

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Retail sales were softer than expected in July, down 1.1% month-over-month. On a year-over-year basis, retail sales were up 15.8% in July versus up 18.7% in June. Year-over-year gains were fueled in part by the drop-off in spending and activity during the pandemic last year. Retail sales have been somewhat uneven during the pandemic due to the timing of fiscal stimulus and economic reopening. Notably, many states stopped providing supplemental pandemic-related unemployment benefits at the end of June, and child tax credit payments were not distributed until the second half of July, which may have impacted spending. We believe the monthly decline in July retail sales also reflects in part consumers' shift in spending toward services, driven by pent-up demand. Additionally, Amazon Prime Day was in June and may have pulled some sales forward (analysts estimate that Amazon recently eclipsed Walmart as the biggest US retailer in terms of sales). The surge in infection rates caused by the Delta variant may have also impacted spending in the month.

Looking ahead, we believe the trajectory of consumer spending will be highly correlated with US labor market conditions; a continued recovery in the labor market should provide a tailwind for consumer spending. However, we believe the resurgence in US virus infection rates may delay the labor market recovery to some extent. Consumer sentiment has also recently declined which does not bode well for the near-term outlook. The savings rate index, which tracks US household savings as a percent of disposable income, remains elevated relative to the longer-term term average (9.4% in June 2021 vs. the 20-year average of 6.7%), but has declined significantly from the peak of 33.8% in April 2020. Meanwhile, household debt as a percent of US GDP is elevated relative to pre-pandemic levels. The end of the federal eviction and foreclosure moratoriums may also be a headwind for consumer spending over the near-term. While there has been roughly $47 billion in pandemic-related fiscal relief allocated for rental assistance, the distribution of those funds to renters and landlords has been slow to materialize, which is something we are watching closely. Overall, as some pandemic-related fiscal relief and policies continue to phase out, we believe the health of the consumer and the trajectory of economic growth will increasingly depend on the labor market (e.g., nonfarm payroll growth and labor force participation).

We expect the bias of the Federal Reserve to remain dovish and highly accommodative over the near-term until there is more clarity on the outlook for employment and inflation. While expectations for Fed tapering before year-end are elevated among market participants, the outlook remains uncertain. We believe a plateau or decline in new US infection rates, continued efficacy of existing vaccines, along with a few more strong employment reports would give the Fed latitude to announce before year-end their intention to begin tapering asset purchases. In the meantime, we expect the tone of Fed Chair Powell to be dovish at next week's Jackson Hole economic symposium. Notably, the theme of this year's symposium is "Macroeconomic Policy in an Uneven Economy" which further suggests to us that the tone of all participating central bankers is likely to be dovish.

Meanwhile, there appears to be a modest slowdown underway in the housing sector, albeit on the heels of a very robust demand environment earlier this year and meaningful year-over-year home price appreciation. Total housing starts fell 7.0% in July to an annual pace of 1,534,000, missing expectations. Single-family starts declined 4.5% in July while multi-family starts fell 13.1%. On a year-over-year basis, housing starts were up just 2.5% in July. The National Association of Home Builders' Housing Market Index dropped five points in August to 75. The index is down from its November 2020 peak of 90 but remains above its long-run average of 50, which is consistent with a modest slowdown in our view. We will get more data on the housing market next week with the existing and new home sales reports for July.

Next Week

Chicago Fed National Activity Index, Existing Home Sales, New Home Sales, Durable Goods, GDP, Personal Income & Outlays, Consumer Sentiment

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